The Investment Engineers

Multi-asset market outlook

Europe takes up the baton

June 2021

For professional investors

Sustainable Investing Expertise by

General overview

Positions: reflation steady as she goes

	Portfolio	Benchmark	Active
Equities Developed Markets	25.00%	25.00%	0.0%
Equities Emerging Markets	5.00%	5.00%	0.0%
Real Estate Equities	5.00%	5.00%	0.0%
SPX (US Equities)	-3.00%	0.00%	-3.0%
STXE 600 (EUR) Pr (Europese aa	2.00%	0.00%	2.0%
Nikkei 225 (Japanese equity)	1.00%	0.00%	1.0%
Commodities	7.50%	5.00%	2.5%
Global treasuries	27.50%	27.50%	0.0%
US Treasuries	-3.50%	0.00%	-3.5%
Investment Grade Corp Bonds	18.00%	20.00%	-2.0%
High Yield Corp Bonds	5.00%	5.00%	0.0%
Emerging Market Bonds LC	5.00%	5.00%	0.0%
Cash	5.50%	2.50%	3.0%

- The dollar came under pressure in May, though this benefitted dollar-sensitive assets such as emerging markets and commodities, which topped the rankings in performance. Gold outshined all other assets during the month, generating a return of more than 7% (in USD). The yellow metal has now almost completely recouped the losses it accumulated during the first months of this year.
- After a few difficult months, developed market government bonds seem to have found a footing. Both high yield and global investment grade bonds delivered positive returns. The top performers within fixed income, however, were inflation linkers, reflecting the pressure that real yields came under in May. Most developed market government bond yields meandered within a narrow range. What was surprising is that German and US 10-years moved in opposite directions: the US bond ended the month lower and the German bond higher.
- We made only small changes to our portfolio in May. We skewed our regional trade in equity markets more towards Europe through lowering our underweight in the US and overweight in Japan, while not adjusting our overweight in Europe. No further changes were made; we are still long on commodities and underweight to investment grade corporate bonds and US Treasuries.

Source: Robeco

Heat Map Asset Returns (in euros)

MULTI ASSET	1mo	3mo	YTD	1YR	3YR	5YR
Gold (USD)	7.3%	9.5%	-0.3%	5.8%	11.8%	8.0%
Oil Index (USD)	5.1%	8.7%	38.0%	79.6%	-19.7%	-9.7%
Global inflation-linked bonds (H, EUR)	1.7%	3.2%	-0.6%	2.7%	3.6%	3.2%
GSCI Commodities (USD)	1.5%	8.4%	26.8%	45.1%	-4.9%	-0.9%
Emerging Markets (LC)	1.3%	2.1%	7.1%	43.9%	10.8%	13.7%
MSCI World local currency	1.0%	9.5%	11.6%	36.9%	13.9%	13.9%
MSCI World (H, EUR)	1.0%	9.4%	11.2%	35.3%	12.0%	12.0%
EMD local currency (UH, EUR)	0.9%	1.9%	-1.9%	8.8%	3.6%	3.1%
EMD hard currency (UH, EUR)	0.9%	0.9%	-2.1%	-1.4%	2.0%	2.7%
Emerging Markets (UH, EUR)	0.7%	2.5%	7.3%	37.4%	8.0%	11.8%
Global high yield (H, EUR)	0.5%	1.5%	1.5%	13.7%	4.0%	4.4%
Global investment grade bonds (H, EUR)	0.4%	0.0%	-2.4%	3.2%	4.0%	2.7%
Global Gov Bonds (H, EUR)	0.1%	-0.2%	-3.3%	-3.0%	2.1%	0.9%
Global real estate (UH, EUR)	0.1%	10.8%	13.6%	17.0%	4.6%	2.9%
Cash (EUR)	0.0%	-0.1%	-0.2%	-0.5%	-0.4%	-0.4%
MSCI World (UH, EUR)	-0.1%	8.9%	11.5%	27.9%	12.7%	12.1%

Equities: Country Indices	1mo	3mo	YTD	1YR	3YR	5YR
India (INR)	6.7%	6.0%	9.2%	62.1%	15.1%	15.7%
Brazil (BRL)	6.2%	14.7%	6.0%	44.4%	18.0%	21.1%
Italy (EUR)	5.2%	11.3%	14.8%	41.5%	8.1%	10.4%
Russia (RUB)	5.0%	11.2%	13.2%	36.1%	17.4%	14.4%
France (EUR)	4.0%	14.8%	18.1%	41.2%	9.0%	10.7%
Spain (EUR)	3.9%	11.7%	14.1%	32.2%	1.8%	3.3%
Switzerland (CHF)	3.3%	11.0%	9.1%	19.0%	13.9%	10.2%
Australia (AUD)	2.3%	8.4%	10.3%	28.0%	9.7%	9.8%
Eurozone (EUR)	2.3%	12.4%	15.3%	35.5%	8.2%	8.3%
Hong Kong (HKD)	2.1%	1.6%	8.1%	31.4%	1.9%	10.8%
Germany (EUR)	1.9%	11.9%	12.4%	33.1%	7.0%	8.5%
Emerging Markets (LC)	1.3%	2.1%	7.1%	43.9%	10.8%	13.7%
Korea (KRW)	1.3%	4.4%	9.9%	59.5%	11.2%	11.9%
UK (GBP)	1.0%	9.6%	10.4%	19.4%	0.9%	6.5%
Global equities (LC)	1.0%	9.5%	11.6%	36.9%	13.9%	13.9%
China (HKD)	0.8%	-4.3%	1.7%	38.7%	8.4%	16.8%
Emerging Markets (EUR)	0.7%	2.5%	7.3%	37.4%	8.0%	11.8%
Asia ex Japan (LC)	0.7%	0.6%	6.6%	45.5%	10.1%	14.3%
USA (USD)	0.6%	10.6%	12.5%	40.2%	18.0%	17.1%
Netherlands (EUR)	0.3%	8.9%	13.6%	33.2%	8.7%	9.6%
Japan (JPY)	0.2%	0.2%	5.9%	34.0%	11.3%	13.0%
Global equities (EUR)	-0.1%	8.9%	11.5%	27.9%	12.7%	12.1%

Fixed Income	1mo	3mo	YTD	1YR	3YR	5YR
Inflation-linked US (UH, USD)	1.2%	2.4%	1.1%	7.1%	6.5%	4.5%
Inflation-linked Europe (EUR)	0.8%	2.3%	1.3%	8.6%	3.4%	2.5%
Investment Grade US (UH, USD)	0.8%	0.1%	-2.9%	3.6%	7.0%	5.0%
EMD local currency (UH, EUR)	0.4%	0.6%	-2.5%	-1.7%	2.6%	2.8%
High Yield US (UH, USD)	0.3%	1.5%	2.2%	15.0%	7.1%	7.4%
US Gov Bonds (H, EUR)	0.2%	-0.4%	-4.0%	-5.1%	2.4%	0.5%
High Yield Europe (EUR)	0.2%	1.4%	2.5%	12.9%	4.4%	4.7%
Global Gov Bonds (H, EUR)	0.1%	-0.2%	-3.3%	-3.0%	2.1%	0.9%
Italy Gov Bonds (EUR)	0.1%	-0.8%	-2.2%	5.9%	6.3%	2.8%
Spain Gov Bonds (EUR)	0.0%	-0.7%	-3.3%	0.6%	3.6%	2.9%
Japan Gov Bonds (H, JPY)	0.0%	0.9%	-0.4%	-1.0%	0.3%	-0.1%
Euro Covered Bonds (EUR)	0.0%	-0.3%	-1.3%	-0.1%	1.2%	0.8%
Europe Senior Financials (EUR)	-0.1%	0.2%	-0.5%	4.7%	2.5%	2.2%
German Gov Bonds (EUR)	-0.1%	-0.9%	-3.3%	-2.3%	1.2%	0.7%
Investment Grade Europe (EUR)	-0.1%	0.1%	-0.8%	4.5%	2.5%	2.2%
Europe Non-financials IG (EUR)	-0.1%	0.0%	-1.0%	4.4%	2.5%	2.1%
France Gov Bonds (EUR)	-0.1%	-1.3%	-4.2%	-1.5%	1.8%	1.3%
EMD hard currency (UH, EUR)	-0.5%	0.2%	-1.2%	-0.5%	4.3%	3.3%

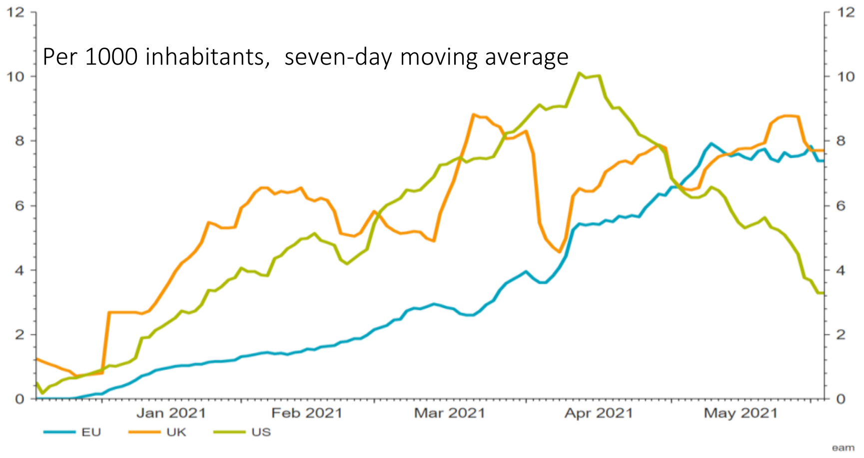
FX versus the EUR	current level	1M	3M	YTD	12M	1m	3m	1yr	1yr
EURO/BRAZIL REAL	6.54	1.1%	1.5%	-3.0%	-8.8%	6.61	6.64	6.01	6.01
EURO/SWISS FRANC	1.10	0.8%	-1.6%	-1.5%	-3.8%	1.11	1.08	1.06	1.06
EURO/SWEDISH KRONA	10.17	0.7%	-0.2%	-1.2%	4.8%	10.24	10.15	10.69	10.69
EURO/NORWEGIAN KRONE	10.00	0.3%	3.7%	4.6%	10.9%	10.03	10.39	11.22	11.22
EURO/CANADIAN DOLLAR	1.48	-0.2%	4.7%	5.0%	3.3%	1.47	1.55	1.53	1.53
EURO/AUSTRALIAN DOLLAR	1.56	-0.9%	1.9%	1.9%	7.4%	1.54	1.59	1.68	1.68
EURO/JAPANESE YEN	131.40	-1.2%	-3.4%	-4.1%	-11.9%	129.86	127.13	117.42	117.42
EURO/CHINA RENMINBI	7.79	-1.3%	0.3%	2.7%	-0.8%	7.69	7.81	7.73	7.73
EURO/SINGAPORE DOLLAR	1.60	-1.4%	0.8%	0.9%	-3.5%	1.58	1.61	1.55	1.55
EURO/SOUTH KOREAN WON	1347.73	-1.7%	0.6%	-1.1%	-3.0%	1325.71	1355.73	1308.08	1308.08
EURO/RUSSIAN RUBLE	90.46	-2.0%	1.7%	0.2%	-11.1%	88.72	91.98	81.44	81.44
EURO/BRITISH POUND	0.87	-2.2%	1.7%	2.6%	0.0%	0.85	0.89	0.87	0.87
EURO/HONG KONG DOLLAR	9.34	-2.4%	0.8%	1.4%	-9.9%	9.12	9.41	8.49	8.49
EURO/INDONESIAN RUPIAH	17473.84	-2.4%	-2.8%	-1.1%	-7.9%	17062.98	16999.98	16194.90	16194.90
EURO/US DOLLAR	1.20	-2.5%	1.0%	1.6%	-9.7%	1.17	1.21	1.10	1.10
EURO/INDIAN RUPEE	89.60	-4.5%	-1.4%	0.2%	-9.7%	85.78	88.40	81.65	81.65

Source: Bloomberg,Robeco

All market data to 31 May, and for US market data, 28 May, unless mentioned otherwise

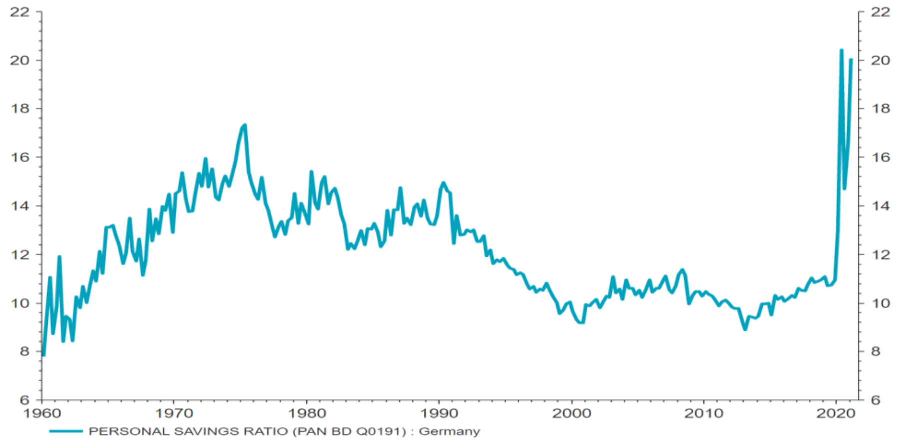
Theme of the month

New Covid-19 vaccinations have reached an inflection point



Source: Refinitiv Datastream , Robeco

Europe has an elevated household saving ratio



Source: Refinitiv Datastream & Robeco

Europe takes up the baton (I)

> After emerging from a double-dip recession, which ended in the first quarter of this year, Europe is now catching up with the recoveries already seen in China and the US. Rising vaccination rates have proven to be the key to unlocking economic activity. Jabs against Covid-19 are still a little behind the US and UK , but the gap is closing as the pace is increasing – about 50% of the population of Germany has now had at least one jab, while the rate is about 40% in France and the Netherlands. The biggest benefit has been the surge in mobility within the developed economies that relaxing the lockdowns has allowed, especially in Europe.

> This of course provides a boost to the service economy. This is reflected in the producer confidence metrics, both from the services and from the goods sector. Some are now at 15-year highs, or even a 17-year high in the case of sentiment in the services sector. So that's really promising also for the subsequent GDP growth numbers which we can expect to see in the second half.

> There are three key elements that underpin the bullishness about European growth. The first and strongest factor is that savings levels are currently very high, and there will be a strong incentive for people to spend this cash when the success of the vaccination programs opens up economies in the second half. The German personal savings rate was 20% in the first quarter, which is historically very elevated. It's logical to assume that people really are eager to spend more on services such as travel when they are able to in the second half. We expect improving retail sales in the Eurozone, which will contribute to consumption growth.

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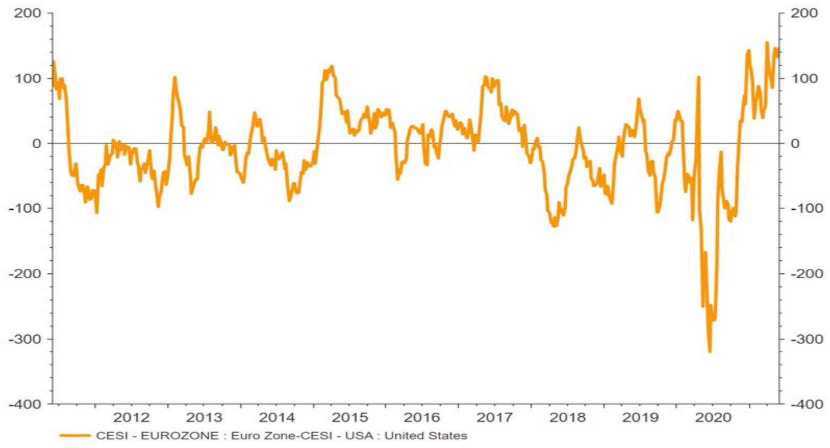
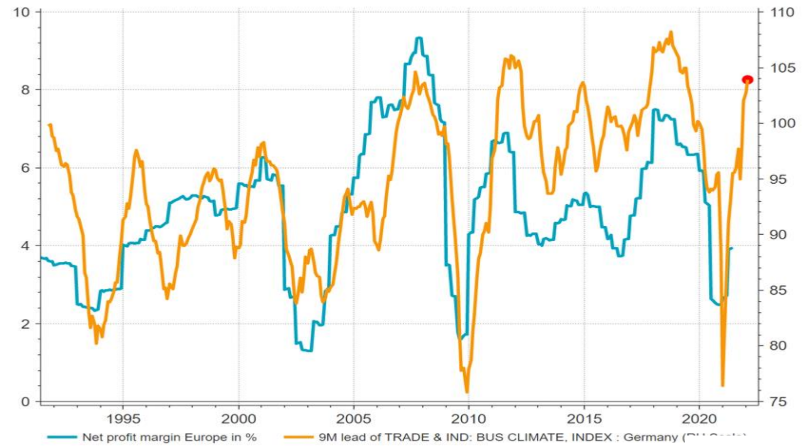
Theme of the month

Macro surprises: Europe is outpacing the US



Source: Refinitiv Datastream & Robeco

Profits are expected to rebound sharply



Source: Refinitiv Datastream , Robeco

Europe takes up the baton (II)

> The second element is that the fiscal thrust in the Eurozone will be with us for somewhat longer. There is now a green light for the disbursements of the EU recovery funds of about EUR 750 billion in grants and loans that will be spread out until about 2026. About 80% of the EU recovery funds will be investment focused and used to improve the structure of the Eurozone economy. The move from emergency support to targeted measures will boost GDP in the peripheral countries. By keeping real interest rates at historically low levels for longer, the ECB will remain a credible fiscal financier which will support a full recovery. Fiscal hawks will have difficulty in pushing for austerity, given that there has been a political swing that has become more populist and left leaning.

> A third element is that global trade is already back to full strength, which will favor Europe. The Eurozone is by and large an open economy, so it has a high sensitivity to global trade activity, especially from China. Although Chinese import demand could slow towards the year end, current manufacturing producer confidence metrics in China signal continuing expansion. We could also see positive spillovers from the strong fiscal and monetary stimulus seen in the US, as the US consumer shifts spending towards European goods and services.

> All this underpins our base case, which is for an environment of continuing economic expansion with rising inflationary pressures. The Eurozone growth trajectory for the remainder of this year and also for the first half of 2022 could deliver further macro surprises to consensus estimates, even as we are already at peak level of relative surprises compared to the US, forcing analysts to upgrade their European forecast vis a vis the US.

Economy (I)

US economy: near-term input price pressures are likely to remain

Source: Refinitiv Datastream & Robeco

Eurozone: economic momentum in Eurozone is accelerating

Source: Refinitiv Datastream & Robeco

> Last month saw a further drop in global Covid-19 cases, with the hotspots – India and Brazil – gradually managing to bring the virus under control as well. The manufacturing sector is still hovering around cyclical peak levels on the back of confidence in the global recovery, with the services sector also showing strong expansion. With over 50% of the population vaccinated, reopening in the US is now well underway, and mobility is almost back to normal. The number of kilometers travelled by private vehicles each week is just 3% below the 2019 average, while freight traffic is already 10% above pre-Covid levels. Air travel will remain at around 85% of the 2019 average for the time being. The ISM purchasing managers' index, which can greatly influence investor and business confidence, confirmed the picture of ongoing expansion.

> The expansion is also continuing in the other developed markets. Germany's IFO Business Climate Index jumped during the month, driven by an uptick in global trade, full order books and optimism in the services sector about a further reopening of the Eurozone economy. At the same time, optimism about the coming six months waned somewhat. This tempered sentiment is being fueled by ongoing supply problems in the goods sector, even though this problem is more acute in the US than in the rest of the developed world. China is another country facing higher input prices as a result of strong global demand for commodities and logistical bottlenecks, particularly in the construction sector. Producer prices in the country rose 6.8% last month. In response to increasing production costs, the Chinese government has introduced measures to discourage speculation in industrial metals.

All market data to 31 May, and for US market data, 28 May, unless mentioned otherwise

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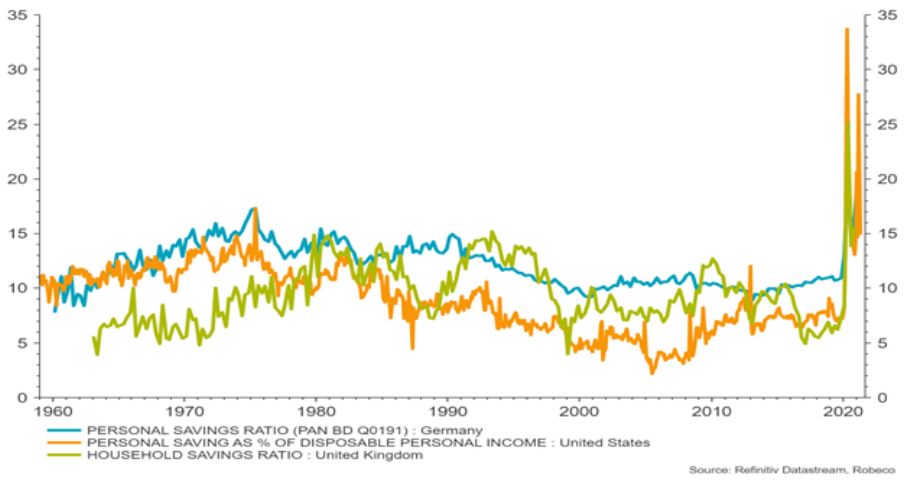
Economy (II)

Elevated savings ratios: pent-up demand is far from exhausted



Source: Refinitiv, Robeco

Historically low real yields underpin the economic recovery in DM

Source: Refinitiv, Robeco

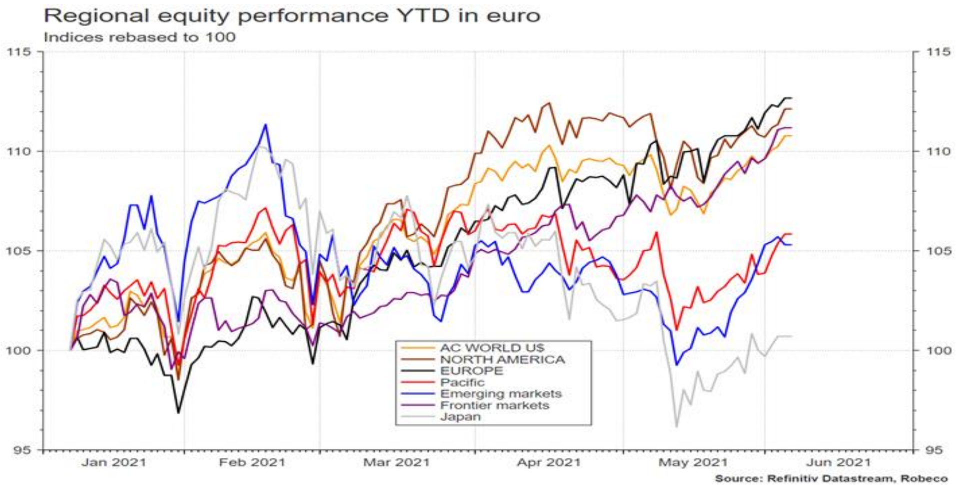
> The Chinese economy also continued to expand, despite lower domestic credit growth.

> Looking forward, we see sufficient support to keep the global economy expanding despite the early-cycle peak in business confidence indicators. Central banks will remain accommodative in the coming period, given the huge hurdle for no longer referring to inflationary pressures as 'temporary'. Although the fiscal stimulus in the US packs less punch, we are seeing a further recovery in the global labor market, with healthy household balance sheets (partly due to asset effects) and increasing investment demand. In the second half of this year, we will also see a further catch-up in consumer demand.

> The so-called 'reflation theme' of accelerating economic growth and rising inflation will, we believe, stand its ground once the market is done testing its validity. There are still tailwinds for the global economy and once the US has reopened, we expect Europe to take up the baton in the second half of 2021. The distribution of money from the EU recovery fund, partial dissaving by European households and growing business investments will lead the way. This will be sufficient to counterbalance a global services sector that will expand at a slower pace in the coming period, also as a consequence of ongoing capacity problems in the commodities sector and semiconductor industry. However, it will not present any immediate danger for companies' profitability, as consumers' high propensity to spend and the current labor underutilization, especially in the US, still enable them to exert sufficient pricing power. At the same time, we also expect markedly higher inflation figures, which will fuel market fears of higher inflation further into the future. Although global growth momentum has peaked, we believe inflation has yet to do so.

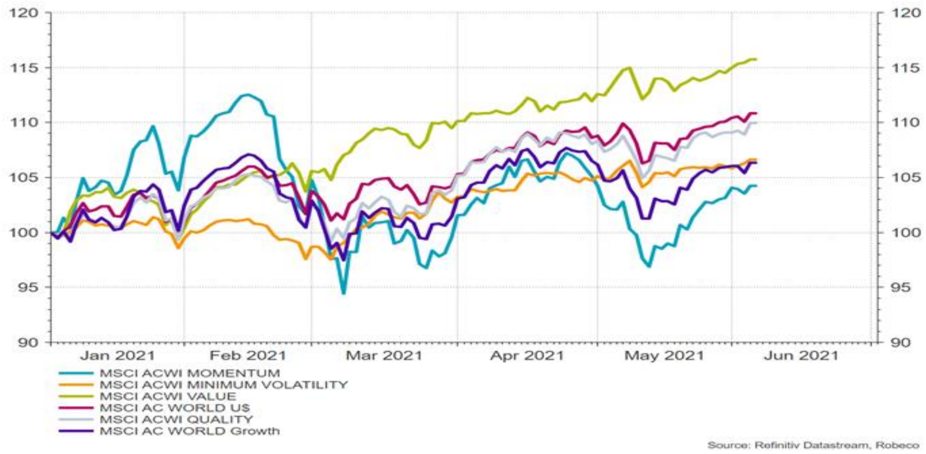
Equities (I)

Regional dispersion: Europe gains while Japan slips



Source: Refinitiv Datastream & Robeco

The momentum style underperforms



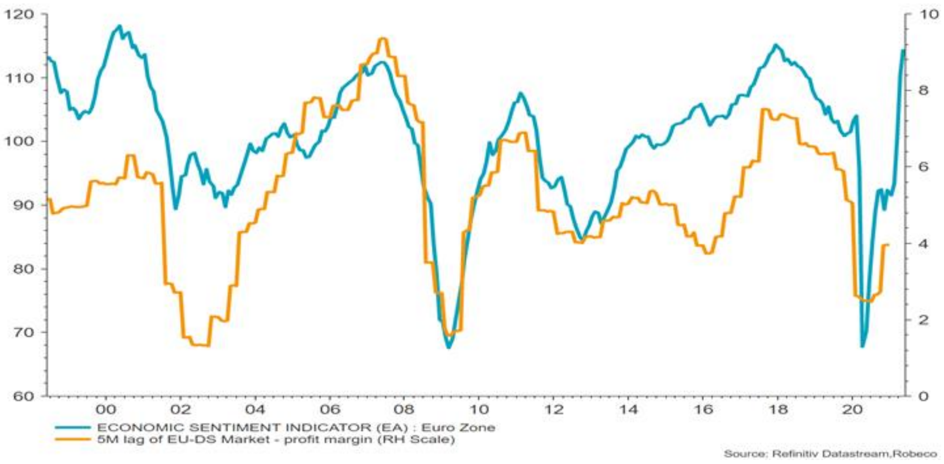
Source: Refinitiv Datastream , Robeco

> In May, the positive momentum for global equities weakened, with the MSCI World index in local currency rising just 1% after a 4% rise in April. The MSCI World index in euros was 11% above the level just prior to the pandemic-related sell-off at the end of May, and increasingly sentiment indicators flashed that the equity rally was due for a correction. Though a typical 10% correction for the broad market has not materialized, the market did show some consolidation, with several regions and sectors like the Nasdaq technology index losing 7.5%, only to recover in the second half of May. Within equity regions, short equity momentum is the strongest for Europe, followed by US equities. Given some exhaustion in broader momentum, the momentum factor within the equity factor universe underperformed last month, while the Value factor continued its relative outperformance despite a flattish yield environment in May. We view momentum as neutral for global equities at this point.

> From a macro perspective, the peak in global activity momentum and elevated inflation fears were the main drivers last month. Given that central banks have been flushing the financial system with liquidity in the wake of the pandemic recession, markets are getting increasingly worried about an inflection point in global excess liquidity as some emerging market central banks already have tightened monetary policy, while the Fed seems to have at least started thinking about tapering given rising US core inflation. Inflation risk is still top of mind for financial markets, though implied inflation expectations have retraced from previous highs in May. The market expects inflation to be transitory in line with recent Fed guidance. Even as the next leg-up in inflation could prove to be somewhat sticky, we do not see an imminent threat to profitability from a further rise in core inflation. Measures of corporate pricing power, like the difference between output and input prices in the US, have accelerated despite the strong rise in input prices.

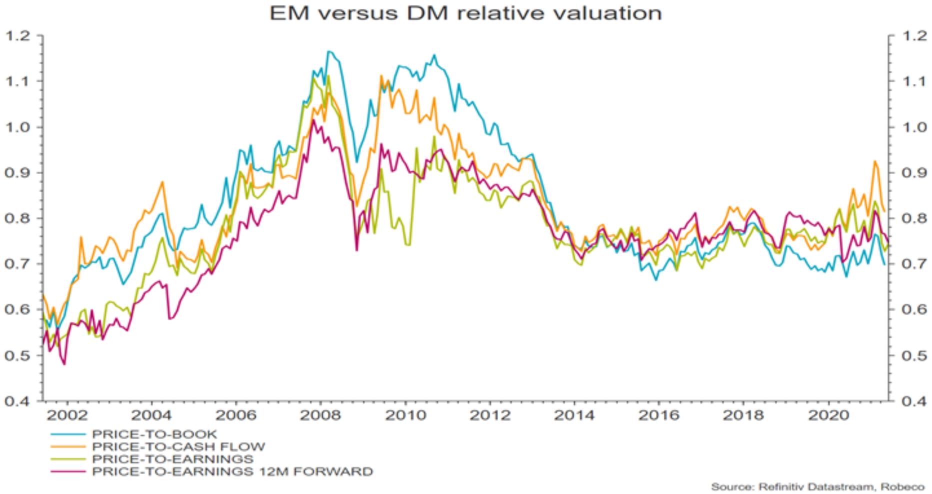
Equities (II)

More upside ahead for European profit margins



Source: Shiller, Robeco

EM equities are cheaper, but not cheap enough



Source: Refinitiv Datastream, Robeco

> In Europe, the rise in the IFO business expectations index suggests further upside for European net profit margins in the near term as well. The first quarter earnings season delivered historically large beats of prior earnings expectations and an 88% overall earnings rebound for the STOXX 600 since last year. This reflationary macro environment remains positive for equities.

> Sentiment cooled in May, evidenced by lower call volumes and a decline in the call/put ratio. However, with the mini correction in popular tech stocks cleaning out excessive risk taking, call volumes have jumped again. In addition, the price to insure against tail risk in the US option markets peaked at 155 and is still above the 140 threshold, flashing near-term correction risk. The irrational exuberance seen around stocks such as AMC also suggests that there are air pockets in this market. Margin debt is high while retail bearishness is very low. In our view, sentiment is a negative for equities, in addition to seasonality.

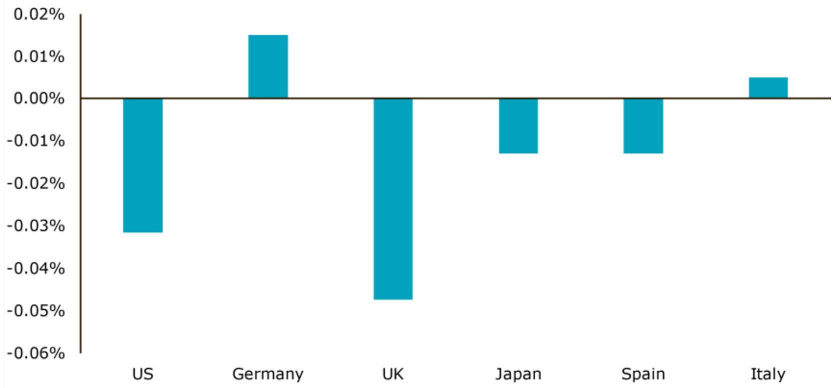
> Valuation levels are historically stretched in the US, though emerging markets have cheapened up recently. To become more constructive on EM equities, we would like to see a weaker dollar, improving GDP differentials and Fed tapering risk to be fully discounted. Though our medium-term outlook remains bullish as we expect a second leg in the reflation trade, we see near-term risk as more balanced, and stay neutral on equities in our multi-asset portfolio, looking to add in case of a dip.

> We are selective risk takers within equities, with an overweight to the value factor and with regional overweights in Europe and Japan, while underweighting US equities. While last month we anticipated a near-term dip in equities, we remain doubtful whether the early May sell-off has delivered a blank sheet for equities to enjoy the second leg of the reflation trade.

All market data to 31 May & for US markets, 28 May, unless mentioned otherwise

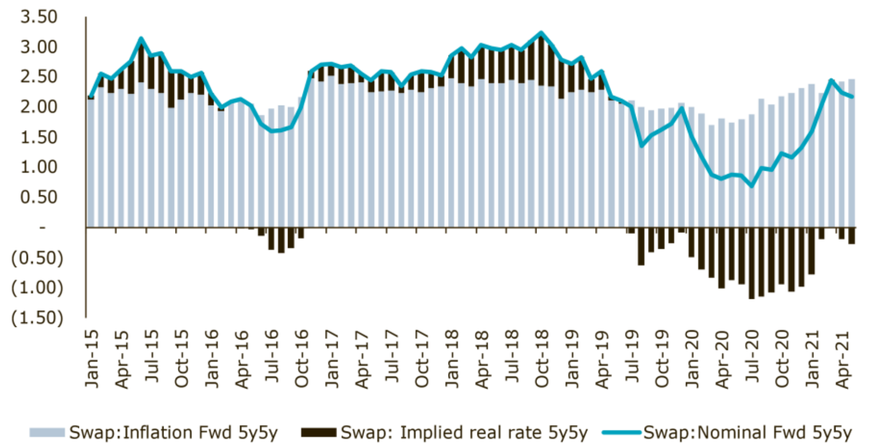
AAA Bonds

10-year yields: narrow ranges but US and Germany diverging



Source: Bloomberg & Robeco

US yields: real rates dragged US yields lower



>Source: Bloomberg & Robeco

- G-10 rates ended the month almost unchanged. During May, both Italian and Spanish rates experienced some upward pressure, but this tapered off as we headed into the month-end. While the moves were marginal, German rates again went in the opposite direction of US rates. The progress that Europe is making with regards to the vaccination roll-out is supporting optimism towards the continent – something that is also being reflected in the economic surprises index. European data has been coming in much stronger than consensus in contrast to US data.
- US 10-years have meandered between 175 and 153 basis points over the past two months. During this time, the evidence that price pressures have building been in the economy has been growing rapidly. The message of the Fed, however, has been consistent: it sees these inflationary pressures as temporarily. The pull lower in rates over the past month was caused by a drop in real rates, as inflation expectations remained relatively stable. The Fed has been very successful in convincing the market that policy change is not imminent, and that the current high inflation numbers are indeed transitory. This is currently almost perfectly reflected in the curve. Whether the market is correct to follow the Fed remains to be seen; what we do know from history is that if the Fed is wrong, and at some point needs to slam on the brakes, this has almost always triggered a recession.
- We continue to think that the current level of the US 10-year is too low. While we acknowledge that the steepness of the curve already indicates that the 10-years will be higher in the future, we still think there is room for the spot 10-years to rise. We therefore remain underweight to 10-year US rates.

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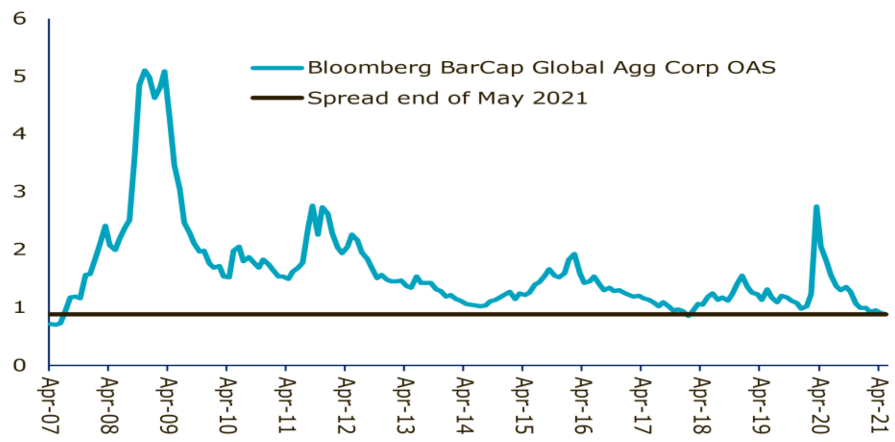
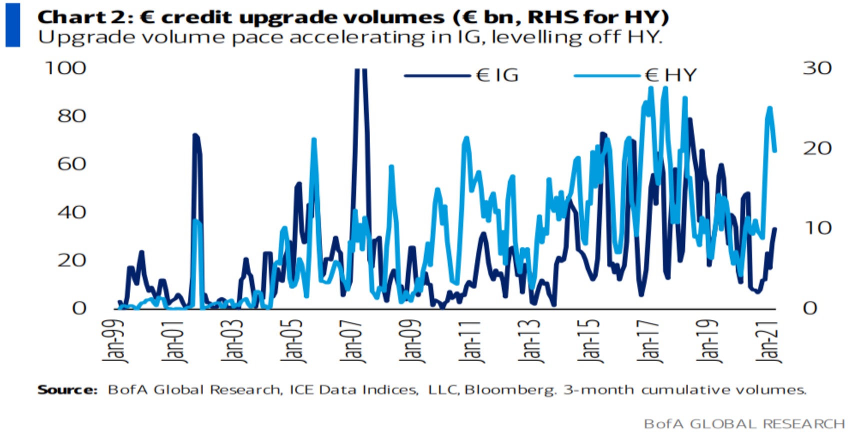
Investment Grade Credits

Investment grade credits are squeezing ever tighter



Source: Bloomberg & Robeco

Investment grade credits: upgrades (volume) are increasing

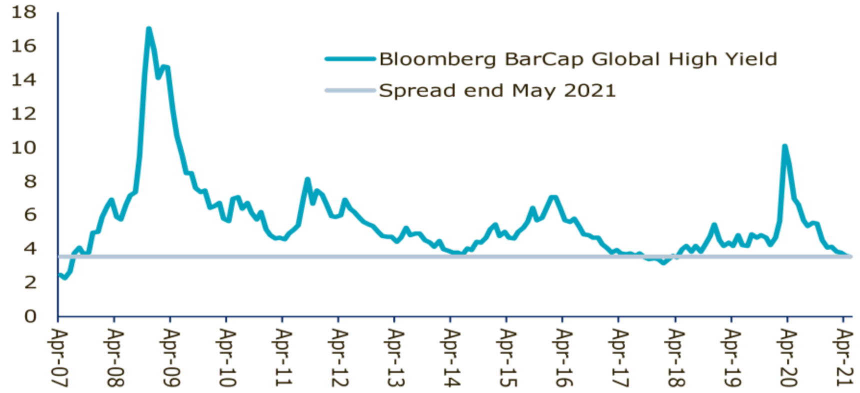


Source: BofA Global Research, ICE Data Indices & Bloomberg

- Global investment grade bonds delivered a positive return this month of just more than 1%. Spreads continued to squeeze tighter and again contributed positively to the overall return. The main driver of the return this month, however, was the interest rate sensitivity of the asset class.
- Given our expectation that government bond yields have not reached their peak yet, we continue to see investment grade corporate bond as one of the least attractive asset classes.
- The improving economic background will continue to be beneficial to assets classes that are geared to the economic cycle. This also bodes well for spreads. In Europe, we saw net upgrades for investment grade. The prospect of reopening the economy now that vaccinations are accelerating will continue to drive this upgrade cycle. However, the fact remains that spreads are already extremely tight, and currently trade at the lowest decile over the past 14 years.
- Duration on the other hand is still in the highest decile of the past 14 years. This puts the asset class at a disadvantage. While improving growth will be beneficial for spreads, it is also a drag due to the currently higher rate sensitivity of the asset class. The buffer that the asset class has to absorb rate rises is too limited in our view.
- Our preference is still for other risky assets such as commodities and value stocks. We therefore remain underweight global investment grade credits. We expect bond yields to continue their increase, with current spread levels offering little buffer.

High Yield

Global high yield spreads continue to tighten



Source: Bloomberg & Robeco

Global high yield issuance

Source: S&P Global ratings

- Global high yield bonds realized a positive return just shy of 1% in May. The average spread level declined to 355 basis points, its lowest level in almost three years.
- The high yield spread ended May practically unchanged from the previous month. During May, the spread moved within a narrow range of roughly 15 basis points, closely tracking the movement of equity volatility. While the Vix ultimately ended the month lower than it started, this was not the case for the high yield spread, though it did reach a new low for the year during May.
- We continue to consider the current backdrop to be constructive for high yield, even though leverage remains high in a historical context, and bond issuance continues at a rapid pace. The current strong earnings recovery and double-digit growth expected for this year opens the door for default rates to drop below average. This is not unusual for the years following a recession. We did, however, notice that lately earnings seems to have become less of a dominant driver for returns of high yield. We continue to see strong earnings as an important factor to keep spreads in check.
- Rising government rates are likely to continue to be a drag on performance. However, the still relatively high spread compared to other bond asset classes enables high yield to better cope with rate rises.
- In addition, even at 355 basis points, there is room for spreads to tighten further, as they are still approximately 50 basis points higher than the lows reached back in 2018.

All market data to 31 May, and for US market data, 28 May, unless mentioned otherwise

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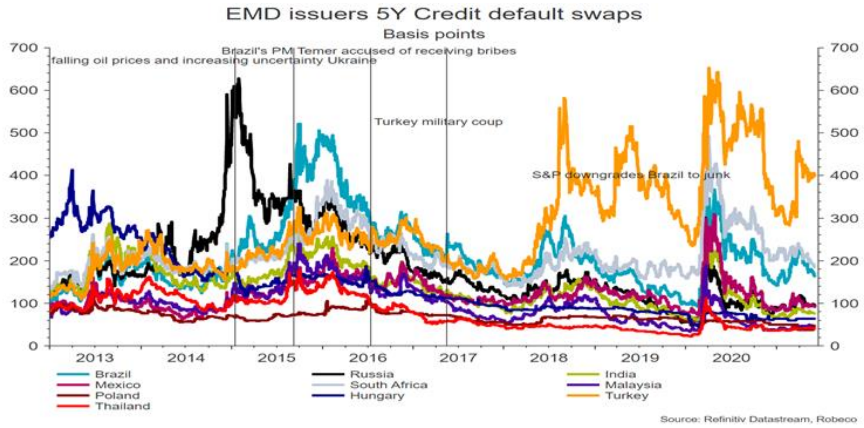
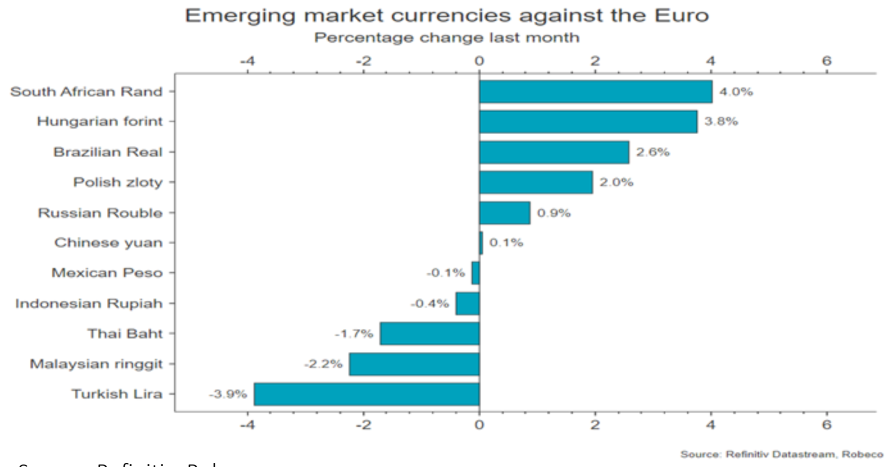
Emerging Market Debt

Emerging market debt in local currency: spread and yield



Source: Refinitiv, Robeco

Emerging market currencies: the Brazilian real is rebounding



Source: Refinitiv, Robeco

> With the rise in Covid-19 cases in emerging markets gradually easing, local currency emerging debt unhedged in euros realized a positive return of 0.4% in May. In the year to date, however, the asset class is still down 2.5% as a result of a relatively slower economic activity rebound compared to developed markets. Rising developed government bond yields also make the relative carry in emerging markets less attractive, while emerging currencies have been declining against the euro.

> Though credit spreads in South Africa, Brazil and notably Turkey remain elevated, spreads for those three countries compressed by over 30 basis points in May, spurred on by a reducing number of Covid-19 cases. Most emerging economies are struggling with record high food inflation, which carries a disproportional weight in CPI baskets. This could create more tightening pressure for emerging market central banks and subsequently slow the pace of the recovery from the pandemic-induced recession. The flip side of rising commodity prices is that current accounts of emerging market debt issuers are improving, sustaining emerging currencies.

> The currency performance and momentum within the EMD (local currency) universe is still dispersed. The South African rand gained 4% in May, while on the other side of the spectrum, the Turkish lira lost another 3.9%. Turkey is experiencing high inflation, with its president very much involving himself in monetary policy matters, arguing for lower interest rates instead to battle inflation.

> We continue to believe that global bond yields can go higher from here, especially as inflation will likely manage to surprise consensus in the near term. The anticipation of Fed tapering could create temporary headwinds for the asset class against an improving fundamental backdrop. We are neutral on local currency emerging market bonds.

All market data to 31 May, and for US market data, 28 May, unless mentioned otherwise

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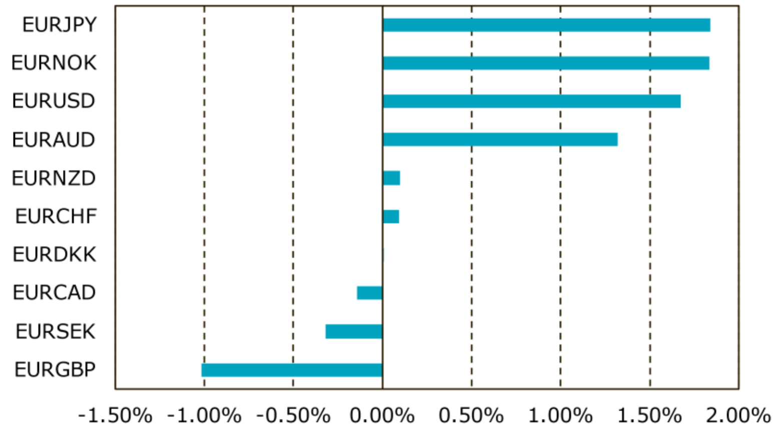
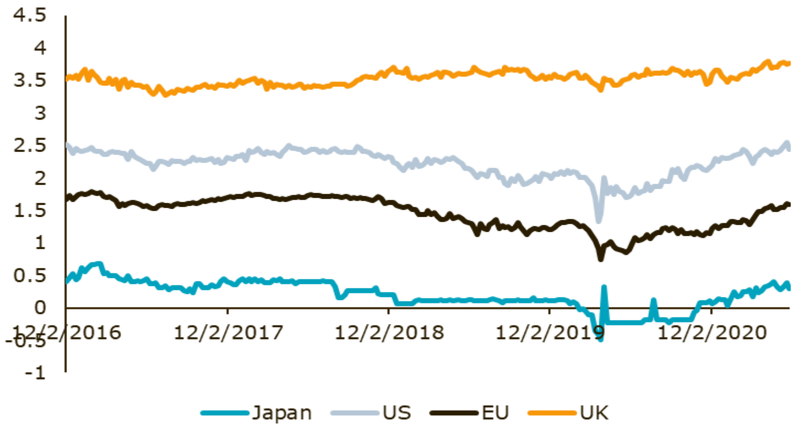
FX

G-10 currencies: sterling is back on top



Source: Bloomberg, Robeco

Inflation expectations (5y/5y) tend to be higher in the UK



>Source: Bloomberg, Robeco

> Sterling was the top performer within the G-10 bucket in May. The passing of local elections, particularly in Scotland, lowered political risk, which allowed risk premiums to compress. While the Scottish National Party did quite well, it failed to get a majority in the popular vote. This is though currently sufficient to keep SNP leader Nicola Surgeon calling for a new independence referendum in the short term. Growth is expected to pick up in the UK, though so will inflation, expectations for which have consistently traded above the 2% target for the past two years. We therefore think that the Bank of England to a certain extent will allow a stronger currency, as this helps curb inflation. The Japanese yen was the weakest currency in May. The combination of a slow vaccination rollout and an increase in outward M&A flows by corporate Japan weighed on the currency.

> In Europe, a sentiment change has become noticeably more optimistic. This more positive tone was visible across several European assets. The spread between 10-year US Treasuries and German bunds narrowed, European equities outperformed US equities and the euro strengthened against the US dollar. We think that the ECB is far away from even considering tapering, given its recent comments. The Fed, however, is getting ever closer to starting the discussion on the topic if the economy continues on its current path of recovery. While the timing will be determined by the employment rate, the pace will be determined by inflation. In the near term, we think the EUR/USD cross will continue to trade within the range its has been in since the third quarter of 2020.

> We currently hold no currency positions.

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